ONTARIO ENERGY CORPORATION

Annual Report 1987

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THE YEAR'S HIGHLIGHTS

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PRESIDENT'S REPORT

In 1987, the Corporation concentrated its efforts on the divestment mandate assigned to it by the Government of Ontario. Limited funds were invested to maintain values and to honour pre-existing commitments to partners, while sales of assets were actively pursued. The Corporation operated with a skeleton staff and minimum overhead while meeting its statutory and legal obligations.

During the fiscal year, the Corporation completed the sale of its western Canadian petroleum interests in joint ventures with Triweb Resources Ltd. and Mannville Oil & Gas Ltd. for a total of $11.3 million in cash. The Ontario Energy Ventures Limited subsidiary succeeded in winding down most of its remaining portfolio through sales and liquidation actions. Ontario Minerals Ltd. was dissolved.

Onexco Oil & Gas Ltd., a subsidiary, signed a letter of intent to sell its two-thirds interest in Trillium Exploration Corporation's frontier oil and gas exploration assets for $22.7 million. Subsequent to the year end, the Corporation devoted much of its efforts to the task of completing this complex transaction. On closing of this sale, the Ontario Energy Corporation will have succeeded in disposing of all its energy assets, except for its 25 per cent equity interest in Suncor Inc. At that point, the Corporation intends to rationalize its structure to reflect this reality.

The Corporation's revenue in 1987 amounted to $2.7 million, while expenses, including wind down costs, depreciation, depletion and royalties were $1.7 million. Income from operations was $1.1 million compared to a loss of $0.8 million the previous year.

The Corporation realized $11.7 million from asset sales in 1987 and reported a net income of $13.0 million. In 1986, a $36.0 million loss, primarily due to write downs, was reported. These asset proceeds left the Corporation in a healthy cash position, so the Board of Directors voted a special dividend of $20.0 million to the Government shareholder.

Recently, several Directors have resigned from the Board to pursue new careers. I would like to acknowledge the distinguished service and contribution of I. Bruce MacOdrum and Dr. Roger Higgin. I would also like to commend the small core of remaining officers and staff of the Corporation whose tenacity and dedication has contributed greatly to the results and performance of the past year.

Respectfully submitted on behalf of the Board:

Duncan M. Allan
President and Chief Executive Officer

BOARD OF DIRECTORS

Duncan M. Allan
Special Advisor to the Premier
Waterfront Development
Province of Ontario

Edward Ciemiega
Director
Legal Services Branch
Ministry of Energy

George A. Dominy
Acting Manager, Policy Development Division
Ministry of Energy

Daniel J. Gagnier
Deputy Minister
Ministry of Energy

Donald S. McColl *
Assistant Deputy Minister
Ministry of Treasury and Economics

Robert A. Simpson *
Assistant Secretary
Management Board of Cabinet

* Member of Audit Committee

OFFICERS

Duncan M. Allan
Chairman
President and Chief Executive Officer

Victor A. Bailey
Treasurer

Robert Law
Secretary

AUDITORS

Deloitte Haskins & Sells

As at June 27, 1988.

FINANCIAL STATEMENTS

PREPARATION AND REVIEW OF THE FINANCIAL STATEMENTS

The financial statements have been prepared by management in accordance with generally accepted accounting principles. Management is also responsible for the other information in the annual report, which is consistent with that contained in the financial statements.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Board exercises its responsibilities through an Audit Committee of the Board, which is composed of directors who are not employees of the Corporation. The Audit Committee meets with management and the external auditors at least twice each year to satisfy itself that management's responsibilities are being properly discharged and to review annually the financial statements.

The external auditors, Deloitte Haskins & Sells, conduct an independent examination, in accordance with generally accepted auditing standards, and express their opinion on the Corporation's financial statements. The auditors' examination includes a review and evaluation of the Corporation's system of internal control. Appropriate tests and other procedures are conducted to provide reasonable assurance that the financial statements are presented fairly. The external auditors have full and free access to the Audit Committee of the Board. The Provincial Auditor has access and reviews from time to time the working paper files of the external auditors.

AUDITORS' REPORT

TO THE SHAREHOLDER OF ONTARIO ENERGY CORPORATION

We have examined the consolidated balance sheet of Ontario Energy Corporation as at December 31, 1987 and the consolidated statements of income and deficit and of changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Corporation as at December 31, 1987 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Deloitte Haskins & Sells

Chartered Accountants
Toronto, Canada
May 24, 1988

CONSOLIDATED STATEMENT OF INCOME AND DEFICIT
Year ended December 31, 1987

	1987	1986
	(000's)	
REVENUE		
Production	$ 1,389	$ 4,279
Interest	1,356	893
	2,745	5,172
EXPENSES		
Depreciation and depletion	736	2,888
General and administrative	656	1,648
Production, operating and royalties	287	1,425
	1,679	5,961
INCOME (LOSS) FROM OPERATIONS	1,066	(789)
WRITE-DOWN OF INVESTMENTS	-	(30,334)
GAIN (LOSS) ON DISPOSAL OF INVESTMENTS	223	(2,972)
EQUITY IN INCOME (LOSS) OF INVESTMENTS (Note 3)	11,750	(2,279)
NET INCOME (LOSS)	13,039	(36,374)
DEFICIT, BEGINNING OF YEAR	(115,209)	(78,835)
DEFICIT, END OF YEAR	$(102,170)	$(115,209)

CONSOLIDATED BALANCE SHEET
December 31, 1987

ASSETS		
CURRENT ASSETS (Note 5)		
Cash and short-term investments	$ 26,022	$ 12,540
Accounts receivable	-	851
	26,022	13,391
INVESTMENTS (Note 2)		
Suncor Inc.	272,419	263,332
Trillium Exploration Corporation	21,773	20,287
Energy resource ventures	-	10,913
Energy technology ventures	548	1,109
	294,740	295,641
FIXED ASSETS	11	8
	$ 320,773	$ 309,040
LIABILITIES		
CURRENT LIABILITIES		
Accounts payable and accrued charges	$ 228	$ 453
Short-term borrowings	-	1,081
	228	1,534
SHAREHOLDER'S EQUITY		
SHARE CAPITAL (Note 4)	97,715	97,715
CONTRIBUTED SURPLUS	325,000	325,000
DEFICIT	(102,170)	(115,209)
	320,545	307,506
	$ 320,773	$ 309,040

Approved by the Board:

Duncan M. Allan, Director

Donald S. McColl, Director

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION
Year ended December 31, 1987

	1987	1986
	(000's)	
OPERATING ACTIVITIES		
Net Income (Loss)	$ 13,039	(36,374)
Suncor Inc. dividends	2,662	3,918
	15,701	(32,456)
Items not affecting cash flow		
Depreciation and depletion	736	2,888
Equity in earnings of investments	(11,750)	2,279
Write-down of investments	-	30,334
(Gain) loss on disposal of investments	(223)	2,972
Other	3	(14)
	4,467	6,003
Changes in operating working capital		
Accounts receivable	851	3,499
Accounts payable and accrued charges	(225)	196
Cash provided by operating activities	5,093	9,698
INVESTING ACTIVITIES		
Trillium Exploration Corporation	(4,086)	(17,062)
Energy resource ventures	(799)	(5,918)
Petroleum Incentives Program Grants	2,656	24,583
Energy technology ventures	(347)	(299)
Proceeds on sale of investments	12,056	2,582
Additions to fixed assets	(10)	-
Cash provided by investing activities	9,470	3,886
FINANCING ACTIVITIES		
Short-term borrowings	(1,081)	(6,469)
INCREASE IN CASH	13,482	7,115
CASH AND SHORT-TERM INVESTMENTS, BEGINNING OF YEAR	12,540	5,425
CASH AND SHORT-TERM INVESTMENTS, END OF YEAR	$ 26,022	$ 12,540

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
December 31, 1987

1. SIGNIFICANT ACCOUNTING POLICIES

The Ontario Energy Corporation has invested in, or otherwise participated in, energy projects with a view to enhancing the availability of energy in Ontario. It has determined to seek prudent disposal of its investments.

Basis of financial statement presentation

The consolidated financial statements include the accounts of the Ontario Energy Corporation and its subsidiaries except Trillium Exploration Corporation ("Trillium"). Trillium is actively involved in an oil and gas exploration program and its operations are not of a financing nature. Accordingly, Trillium is accounted for using the equity method because consolidating the accounts would not be more informative.

The investment in Suncor Inc. and certain other investments are accounted for using the equity method.

The Corporation conducts substantially all of its oil and gas exploration and production activities on a joint venture basis, and accordingly the accounts reflect the Corporation's investment in such activities.

The full-cost method of accounting is used to account for the Corporation's direct investments in oil and gas exploration activities whereby all costs of exploring for and developing oil and gas reserves are capitalized.

Fixed assets

Furniture and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is determined using the straight-line method over a period of 60 months.

Income taxes

The Corporation and its wholly-owned direct subsidiaries and their wholly-owned direct subsidiaries are not subject to income tax so long as not less than 90 per cent of the outstanding shares of the Corporation are held directly by the Province of Ontario. All of the Corporation's outstanding shares are presently held by the Province of Ontario. Onexco Oil & Gas Ltd., which is a wholly-owned indirect subsidiary of the Corporation, is subject to income taxes.

2. INVESTMENTS

Suncor Inc.

The investment in 25% of the shares of Suncor Inc. is accounted for using the equity method.

2. INVESTMENTS (continued)

Summarized financial information of Suncor Inc. as at December 31 is as follows:

	1987	1986
	(in millions)	
Financial Information		
Working capital	$ 37	$ 74
Total assets	$ 2,080	$ 2,107
Shareholders' equity		
Preferred shares	$ 7	$ 7
Common shares and retained earnings	1,090	1,053
	$ 1,097	$ 1,060
Operations		
Revenue	$ 1,370	$ 1,157
Net income (loss)	$ 48	$ (7)
Cash dividends on common shares	$ 10	$ 16
Stock dividends on common shares	11	10
	$ 21	$ 26

In 1985 certain companies instituted an action against Suncor Inc. disputing their obligation to pay an overriding royalty to Suncor. The amount of disputed royalty revenues recorded by Suncor to December 31, 1987 is approximately $26 million before taxes, including $3 million in 1987. Any material adverse financial impact on Suncor Inc., including interest, resulting from this action will be applied retroactively to the periods affected.

Trillium Exploration Corporation

The Corporation has a two-thirds interest in Trillium which was formed to explore for oil and gas in the frontier areas of Canada. Trillium has had no income or loss from operations.

Subsequent to the year end, the Corporation accepted a purchase offer for its investment in Trillium Exploration Corporation for cash of approximately $22 million, which approximates the year-end carrying value.

Energy technology ventures

The Corporation has investments in energy technology ventures of various types, typically in the form of a minority equity interest or debt. These investments are reflected at the lower of cost and estimated net realizable value.

3. EQUITY ADJUSTMENT IN INVESTMENTS

Equity adjustment in investments reflects the Corporation's share of the income or loss of Suncor Inc. which is accounted for using the equity method.

4. SHARE CAPITAL

Share capital - December 31, 1987 and 1986	
Authorized	
An unlimited number of common shares	
20,000,000 non-voting special shares	
Issued	
2,000,000 common shares	$ 100,000
Less	
45,708 common shares held in Treasury, at cost	2,285
	$ 97,715

5. SUBSEQUENT EVENT

On March 24, 1988 the Directors declared a cash dividend in the aggregate amount of $20,000,000 payable to the Shareholder on March 31, 1988.